

## NOTICES OF FINAL RULEMAKING

The Administrative Procedure Act requires the publication of the final rules of the state's agencies. Final rules are those which have appeared in the Register first as proposed rules and have been through the formal rulemaking process including approval by the Governor's Regulatory Review Council. The Secretary of State shall publish the notice along with the Preamble and the full text in the next available issue of the *Arizona Administrative Register* after the final rules have been submitted for filing and publication.

### NOTICE OF FINAL RULEMAKING

#### TITLE 18. ENVIRONMENTAL QUALITY

#### CHAPTER 2. DEPARTMENT OF ENVIRONMENTAL QUALITY AIR POLLUTION CONTROL

##### PREAMBLE

1. **Sections Affected**

R18-2-102	<b><u>Rulemaking Action</u></b>
R18-2-210	Amend
R18-2-327	Amend
R18-2-333	Amend
R18-2-901	Amend
R18-2-1101	Amend
Appendix 2	New Appendix
2. **The specific authority for the rulemaking, including both the authorizing statute (general) and the statutes the rule are implementing (specific):**

Authorizing statute: A.R.S. § 49-104  
Implementing statute: A.R.S. § 49-425
3. **The effective date of the rules:**

December 7, 1995
4. **A list of all previous notices appearing in the Register addressing the final rule:**

**Notice of Rulemaking Docket Opening:**  
1 A.A.R. 1669 , September 22, 1995

**Notice of Proposed Rulemaking:**  
1 A.A.R. 1653 , September 22, 1995
5. **The name and address of agency personnel with whom persons may communicate regarding the rule:**

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6. **An explanation of the rule, including the agency's reasons for initiating the rule:**

The Arizona Department of Environmental Quality (ADEQ) is updating its current air quality rules regarding New Source Performance Standards (NSPS) and National Emissions Standards for Hazardous Air Pollutants (NESHAP), in order to obtain delegated authority to enforce recent federal regulations. The federal regulations implement Sections 111 and 112 of the Clean Air Act Amendments of 1990.

These federal standards are designed to reduce air pollution generated by stationary sources. NSPS regulates emissions of the 6 criteria pollutants (carbon monoxide, ozone, oxides of nitrogen, lead, sulfur dioxide, and particulate matter). NESHAP regulates emissions of the 189 hazardous air pollutants (HAPs) listed in the Clean Air Act, Section 112.

This rulemaking updates through July 1, 1995, the portions of federal rule that the state wishes to have the authority to enforce. Several portions, such as those governing radionuclides, are not adopted by ADEQ since they are enforced by the Radiation Regulatory Agency.

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This final rulemaking also updates other ADEQ rules that incorporate by reference Sections of the Code of Federal Regulations (CFR), as well as updating testing methods and emission factors.

Specifically, the following matters are incorporated by reference:

**New Source Performance Standards (NSPS) for Automobile and Light-Duty Truck Surface Coating Operations (40 CFR 60, Subpart MM):** Amended on October 11, 1994 (59 Fed.Reg. 51383). This revised NSPS does not reflect a change in the basis of the standard for coatings but reflects a better understanding of the performance of the prime coating system and prime coat materials upon which the standard was originally based. The intended effect of this NSPS, according to EPA, is to require all new, modified, and reconstructed prime coat operations at automobile and light-duty truck assembly plants to use the best demonstrated system of continuous emission reduction considering costs, non-air quality health, environmental, and energy impacts. The revised NSPS is consistent with the performance of the best demonstrated prime coating system and prime coat materials.

**New Source Performance Standards (NSPS), 40 CFR 60, Appendix A:** Amended on December 6, 1994 (59 Fed.Reg. 62924). The amended federal appendix adds Method 25E - Determination of Vapor Phase Organic Concentration in Waste Samples.

**National Emission Standards for Hazardous Air Pollutants (NESHAPs) for Source Categories: General Provisions (40 CFR 63, Subpart A):** Promulgated on March 16, 1994 (59 Fed.Reg. 12408). The General Provisions in Part 63 codify general procedures and criteria to implement emission standards for stationary sources that emit (or have the potential to emit) one or more of the 189 hazardous air pollutants (HAPs) listed in Section 112 of the Clean Air Act. Standards for individual source categories are being developed separately and are codified in other subparts of 40 CFR 63. When sources become subject to standards established for individual source categories, the sources also must comply with the requirements of the General Provisions, except when specifically overridden by the standards. The federal rulemaking also included changes to the General Provisions for 40 CFR 60 and 61, where appropriate, to make them consistent with 40 CFR 63.

**National Emission Standards for Organic Hazardous Air Pollutants from the Synthetic Organic Chemical Manufacturing Industry (Also known as "Hazardous Organic NESHAP" or "HON") (40 CFR 63, Subparts F, G, H, and I):** Promulgated on April 22, 1994 (59 Fed. Reg. 19402); and amended on June 6, 1994; September 20, 1994; October 24, 1994; October 28, 1994; January 27, 1995; and April 10, 1995. The rule applies to production of 386 out of approximately 660 chemical substances produced by synthetic organic chemical manufacturing industries (SOCMI) as commercial products. To be subject to the rule, a chemical process must be located at a major source (a plant site that collectively emits more than 10 tons per year of any 1 hazardous air pollutant (HAP) or more than 25 tons per year of multiple HAPs). In addition, to be subject, this process must also manufacture 1 or more SOCMI chemicals listed in the rule and have an organic HAP as either: (1) a product, by-product, co-product, or intermediate; or (2) a reactant.

**National Emission Standards for Hazardous Air Pollutants: Hard and Decorative Chromium Electroplating and Chromium Anodizing Tanks (40 CFR 63, Subpart N):** Promulgated January 25, 1995 (60 Fed.Reg. 4948) and amended on May 24, 1995, and June 27, 1995. Nationally, there are an estimated 1,500 hard chromium electroplating facilities, 2,800 decorative chromium electroplating facilities; and 700 chromium anodizing facilities that will be affected by the federal regulation. Hard chromium electroplated parts include large cylinders and industrial rolls used in construction equipment and in printing presses; decorative chromium plated parts include appliances such as toasters, various hand tools, and automotive parts; anodized parts include miscellaneous aircraft parts, including wings and landing gears. The vast majority of the facilities covered by this rule electroplate parts for other industry manufacturers. The Maximum Achievable Control Technology (MACT) for chromium electroplaters and anodizers is designed to limit the emissions of hexavalent chromium, a known carcinogen. This rule will cover all processes that plate metals with chromium using bath-type process tanks.

**National Emission Standards for Hazardous Air Pollutants: Ethylene Oxide Emissions Standards for Sterilization Facilities (40 CFR 63, Subpart O):** Promulgated December 6, 1994 (59 Fed.Reg. 62585). Sources affected by the rule include medical equipment suppliers, pharmaceuticals, other health-related industries, spice manufacturers, large libraries, large museums and archives, and contract sterilizers. Products that are sterilized with ethylene oxide include medical equipment, spices, cosmetics, and pharmaceuticals. Libraries, museums, and archives use ethylene oxide as a fumigant to control insects and microorganisms on fragile historical materials, although many of these entities in Arizona have phased out the use of ethylene oxide, due to its potential for adverse health effects.

**National Emission Standards for Hazardous Air Pollutants: Industrial Process Cooling Towers (40 CFR 63, Subpart Q):** Promulgated September 8, 1994 (59 Fed.Reg. 46339). Industrial process cooling towers remove heat from chemical and industrial processes. Water treatment chemicals, such as chromium, are added to cooling tower waters to protect equipment and piping from corrosion, and to control algae growth in the tower. Chromium emissions are released into the atmosphere from the cooling tower during the cooling process. Sources, such as petroleum refineries, chemical manufacturing plants, and primary metal producers, that operate industrial process cooling towers using chromium-based water treatment chemicals will be affected by the regulation. Industrial process cooling towers that are used exclusively for cooling, heating, ventilation, and air conditioning systems, which are referred to as comfort cooling towers, are not covered by this rule.

**National Emission Standards for Hazardous Air Pollutants: Halogenated Solvent Cleaning (40 CFR 63, Subpart T):** Promulgated on December 2, 1994 (59 Fed.Reg. 61801) and amended on December 30, 1994 and June 5, 1995. The federal regulation employs a combination of equipment and operational practices. The standards for all batch vapor and in-line units and are based on Maximum Achievable Control Technology (MACT) as EPA found no justification for using Generally Available Control Technology (GACT) for area sources. Standards for batch cold cleaning machines are based on GACT. The standards for halogenated HAP solvent cleaning machines apply to each individual solvent cleaning machine that uses any solvent containing methylene chloride, perchloroethylene, trichloroethylene, 1,1,1-trichloroethane, carbon tetrachloride or chloroform, or any combination of these halogenated HAP solvents, in a total concentration that is greater than 5% by weight.

**National Emission Standards for Hazardous Air Pollutants: Epoxy Resins Production and Non-Nylon Polyamides Production (40 CFR 63, Subpart W):** Promulgated March 8, 1995 (60 Fed.Reg. 12670). The federal regulation limits emissions of hazardous air pollutants (HAPs) from existing and new facilities that manufacture epoxy resins and non-nylon polyamide resins. The standards are based on the EPA's determination of July 16, 1992 (57 Fed.Reg. 31576) that epoxy resins and non-nylon polyamide resins manufacturing generate significant emissions of certain HAPs, primarily epichlorohydrin.

**National Emission Standards for Hazardous Air Pollutants: Secondary Lead Smelting (40 CFR 63, Subpart X):** Promulgated June 23, 1995 (60 Fed.Reg. 32587). The rule will affect secondary lead smelters that use blast, reverberatory, rotary, or electric smelting furnaces to recover lead metal from scrap lead, primarily from used lead-acid automotive-type batteries.

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**National Emission Standards for Hazardous Air Pollutants: Magnetic Tape Manufacturing Operations (40 CFR 63, Subpart EE): Promulgated December 15, 1994 (59 Fed. Reg. 64593).** Nationally, of the 25 plants that manufacture magnetic tape, 14 are estimated to be major sources of air toxics and thus affected by the regulation. At least 1 such source is located in Arizona. Types of products made by this industry include audio and video cassettes and computer diskettes. The industry is geographically widespread across the country. The MACT for magnetic tape manufacturing operations is designed to limit the emissions of a number of federal HAPs, including those in the wastewater stream if they are part of the tape manufacturing process.

The update in this final rulemaking to R18-2-210 includes the designation of the non-attainment areas for Bullhead City and Payson for PM10 (particulate matter measuring 10 microns or less) (58 Fed. Reg. 67341, December 21, 1993).

The updates to R18-2-327 cover amendments to the certification of continuous emissions monitors under the federal Acid Rain Program (40 CFR 75, Subpart C). EPA has revised and clarified the existing certification procedures, specifically including loss of provisional certification, audit decertification, certification and use of backup monitors, and notifications for recertification. The amendments to R18-2-327 also incorporate the newest edition of EPA publication "AP-42" which contains the emissions factors relied on by ADEQ.

The update to R18-2-333 covers minor technical corrections to the federal Acid Rain Permitting program described in 40 CFR 72. New Appendix 2 includes all test methods currently relied upon by ADEQ. This Appendix represents a collection of test methods already incorporated elsewhere in 18 A.A.C. 2, with the addition of federal test methods found in 40 CFR 51, Appendix M. This year's federal update to Part 51, Appendix M, was **Test Method 205**, designed to be used to verify the performance and accuracy of gas dilution systems during a field test. It was promulgated on May 30, 1995 (60 Fed. Reg. 28052) and is a flexible alternative to some of the test methods required under 40 CFR 60.

In R18-2-102, the incorporation by reference date for all other miscellaneous references to 40 CFR is being amended to July 1, 1995. This reflects changes in text, grammar corrections spelling corrections and other changes that are not substantial in nature.

Docket Location: Materials relevant to this rulemaking are contained in ADEQ Rule Docket No. Air-13. The docket is located on the 8th Floor at the Arizona Department of Environmental Quality, 3033 North Central, Phoenix, Arizona. The docket may be inspected from 8 a.m. to 5 p.m., Monday through Friday.

**7. A showing of good cause why the rule is necessary to promote a statewide interest if the rule will diminish a previous grant of authority to a political subdivision of this state:**

Not applicable. The 3 counties having jurisdiction over air pollution separately from ADEQ, pursuant to A.R.S. Title 49 (Maricopa County, Pima County, and Pinal County) will each incorporate by reference the same rules incorporated in this rulemaking, at a later time.

**8. The summary of the economic, small business, and consumer impact:**

The purpose in adopting the federal regulations for NSPS and NESHAP is to meet the criteria for federal delegation to ADEQ to implement and enforce these standards. When the standards are embodied in state rule, they are implemented and enforced by state personnel. There is no added impact to regulated entities. The primary duty of enforcement simply shifts from the EPA to ADEQ. Federal NSPS and NESHAP regulations are enforceable in Arizona under federal law on the effective date of the regulations, regardless of whether they are adopted as state rule.

State adoption of effective federal regulations does not impose standards or requirements on private entities. Therefore, the economic impact to the regulated community from the state adoption of these rules is zero.

The cost to ADEQ is negligible. This is because ADEQ expects to continue its enforcement of all incorporated federal regulations and the addition of these few is not expected to add any additional measurable impacts. On the contrary, it would add complexity and some administrative cost to selectively not enforce 1 particular subset of federal regulations and instead to establish a partnership with EPA so that EPA could manage those enforcement actions.

The methodology used to reach this assessment involved a coordinated search among ADEQ staff to find the number of entities affected by the rulemaking, followed by a determination of the amount of public outreach, education, and compliance efforts that would be required to effectively implement the federal regulations being incorporated. Most of the incorporated standards affect fewer than 5 entities regulated by ADEQ; even in the case of chromium electroplaters, which touches hundreds of business enterprises in Arizona, only 2 or 3 are within the jurisdiction of ADEQ. Maricopa County and Pima County, as independent air quality jurisdictions, will have the heaviest administrative burdens as a result of the federal rulemakings.

Substantial benefits are realized when primary regulatory authority rests with the state as opposed to the federal government, both for the regulated community and the general public. There is usually better communication and improved understanding when facilities work with state regulators rather than with federal authorities, since they are more likely to meet in person and to understand specific business and geographic circumstances. Enforcement by the state allows more efficient processing of permits, complaints, and other related issues.

The benefits of state versus federal regulatory authority are magnified with respect to small businesses, since ADEQ has an easily accessible Small Business Assistance Program for air quality, which the EPA does not have in this state.

There is no direct impact on consumers, due to the analysis given above.

**9. A description of the changes between the proposed rules, including supplemental notices, and final rules (if applicable):**

One written comment was received on this rulemaking. The commenter requested that the incorporation by reference of the Gasoline Distribution Facilities standard in R18-2-1101 be delayed, since the federal regulation being incorporated was being revised by the U.S. Environmental Protection Agency (EPA).

The Gasoline Distribution Facilities standard, as incorporated in this rulemaking, would have set a notification deadline for the facilities of December 1995, and a compliance deadline of December 1996. The EPA will revise this federal regulation in November 1995 to move these deadlines 1 year into the future. The notification deadline will be set at December 1996, and the leak detection and repair deadline will be postponed until December 1997.

The Department, after independent contacts with the EPA, agrees with the commenter and has deleted the standard from its rulemaking. A new ADEQ rulemaking will be proposed after November of this year, to incorporate the newly-revised Gasoline Distribution standard.

The proposed rule reads as follows:

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**"R18-2-1101. National Emission Standards for Hazardous Air Pollutants (NESHAP)**

A. ...

B. ...

13. Subpart R - Gasoline Distribution Facilities (Bulk Gasoline Terminals and Pipeline Breakout Stations).

..."

The adopted rule reads as follows:

**"R18-2-1101. National Emission Standards for Hazardous Air Pollutants (NESHAP)**

A. ...

B. ...

13. Subpart R - Gasoline Distribution Facilities (Bulk Gasoline Terminals and Pipeline Breakout Stations).

..."

The remaining subsections have been renumbered to conform.

**10. A summary of the principal comments and the agency response to them:**

Please see the section above regarding changes made to the proposed rule.

**11. Any other matters prescribed by statute that are applicable to the specific agency or to any specific rule or class of rules:**  
Not applicable.

**12. Incorporations by reference and their locations in the rules:**

All CFR references (R18-2-102); 40 CFR 81.303 (R18-2-210); EPA Publication AP-42 (R18-2-327), 40 CFR 72 (R18-2-333); 40 CFR 60 (R18-2-901); 40 CFR 61 and 63 (R18-2-1101); and test methods in 40 CFR 51, 60, 61, 63 and 75 (Appendix 2).

**13. Was this rule previously adopted as an emergency rule?**

No.

**14. The full text of the rules follows:**

**TITLE 18. ENVIRONMENTAL QUALITY**

**CHAPTER 2. DEPARTMENT OF ENVIRONMENTAL QUALITY  
AIR POLLUTION CONTROL**

**ARTICLE 1. GENERAL PROVISIONS**

R18-2-102. Incorporated Materials

**ARTICLE 2. AMBIENT AIR QUALITY STANDARDS;  
AREA DESIGNATIONS; CLASSIFICATIONS**

R18-2-210. Attainment, Nonattainment, and Unclassifiable  
Area Designations

**ARTICLE 3. PERMITS AND PERMIT REVISIONS**

R18-2-327. Annual Emissions Inventory Questionnaire

R18-2-333. Acid Rain

**ARTICLE 9. NEW SOURCE PERFORMANCE STANDARDS**

R18-2-901. Standards of Performance for New Stationary  
Sources

**ARTICLE 11. FEDERAL HAZARDOUS AIR POLLUTANTS**

R18-2-1101. National Emission Standards for Hazardous Air  
Pollutants (NESHAPs)

**A2. APPENDIX 2. REPEALED TEST METHODS AND  
PROTOCOLS**

**ARTICLE 1. GENERAL PROVISIONS**

**R18-2-102. Incorporated Materials**

The following documents are incorporated by reference and are on file with the Office of the Secretary of State and the Department:

1. The Department's "Arizona Testing Manual for Air Pollutant Emissions," amended as of March 1992 (and no future editions).

2. All ASTM test methods referenced in this Chapter as of the year specified in the reference (and no future amendments). They are available from the American Society for Testing and Materials, 1916 Race Street, Philadelphia, Pennsylvania 19103-1187.

3. All parts of the CFR referenced in this Chapter. They are published in 40 CFR, amended as of July 1, 1991 1995 (and no future amendments), except as otherwise specifically provided in ~~R18-2-210, R18-2-901 and R18-2-1101~~. They are available from the U.S. Government Printing Office, Superintendent of Documents, Mail Stop SSOP, Washington, D.C. 20402-9328.

4. The U.S. Government Printing Office's "Standard Industrial Classification Manual, 1987" (and no future editions).

**ARTICLE 2. AMBIENT AIR QUALITY STANDARDS;  
AREA DESIGNATIONS; CLASSIFICATIONS**

**R18-2-210. Attainment, Nonattainment, and Unclassifiable Area Designations**

40 CFR 81.303 as amended as of July 1, 1992 1995 (and no future editions) is incorporated herein by reference and is on file with the Department of Environmental Quality and the Office of Secretary of State.

**ARTICLE 3. PERMITS AND PERMIT REVISIONS**

**R18-2-327. Annual Emissions Inventory Questionnaire**

- A. Every source subject to a permit requirement under this Chapter shall complete and submit to the Director an annual emissions inventory questionnaire. The questionnaire is due by March 31 or 90 days after the Director makes the inventory form available, whichever occurs later, and shall include emission information for the previous calendar year. These requirements apply whether or not a permit has been issued and whether or not a permit application has been filed.

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B. The questionnaire shall be on a form provided by the Director and shall include the following information:

1. The source's name, description, mailing address, contact person and contact person phone number, and physical address and location, if different than the mailing address.
2. Process information for the source, including design capacity, operations schedule, and emissions control devices, their description and efficiencies.
3. The actual quantity of emissions from permitted emission points and fugitive emissions as provided in the permit, including documentation of the method of measurement, calculation or estimation, determined pursuant to subsection (C) of the following regulated air pollutants:
  - a. Any single regulated air pollutant in a quantity greater than 1 ton or the amount listed for the pollutant in subsection (a) of the definition of "significant" in R18-2-101, whichever is less.
  - b. Any combination of regulated air pollutants in a quantity greater than 2\$ tons.

C. Actual quantities of emissions shall be determined using the following emission factors or data:

1. Whenever available, emissions estimates shall either be calculated from continuous emissions monitors certified pursuant to 40 CFR 75, Subpart C and referenced appendices, ~~as published in the Federal Register on January 11, 1993 (and no later editions) which is incorporated herein by reference, and is on file with the Department and the Secretary of State, or data quality assured pursuant to Appendix F of 40 CFR 60.~~
2. When sufficient data pursuant to subsection (C)(1) is not available, emissions estimates shall be calculated from data from source performance tests conducted pursuant to R18-2-312 in the calendar year being reported or, when not available, conducted in the most recent calendar year representing the operating conditions of the year being reported.
3. When sufficient data pursuant to subsection (C)(1) or (C)(2) is not available, emissions estimates shall be calculated using emissions factors from EPA Publication No. AP-42 "Compilation of Air Pollutant Emission Factors", Volume I: Stationary Point and Area Sources, ~~Fourth Fifth Edition, supplements A through F, 1985 1995, U.S. Environmental Protection Agency, Research Triangle Park, N.C. (GPO Order No. 055-000-00251-7), (and no future editions) which is incorporated herein by reference and is on file with the Department of Environmental Quality and the Office of Secretary of State. AP-42 can be obtained from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402, telephone (202) 783-3238, or by downloading the document from the EPA Technology Transfer Network, computer modem number (919) 541-5742, setting 8-N-1, VT100 or ANSI.~~
4. When sufficient data pursuant to subsections (C)(1) through (C)(3) is not available, emissions estimates shall be calculated from material balance using engineering knowledge of process.
5. When sufficient data pursuant to subsections (C)(1) through (C)(4) is not available, emissions estimates shall be calculated by equivalent methods approved by the Director. The Director shall only approve methods that are demonstrated as accurate and reliable as the

applicable method in paragraphs (1) through (4) of this subsection.

- D. Actual quantities of emissions calculated under subsection (C) shall be determined on the basis of actual operating hours; production rates; in-place process control equipment; operational process control data; and types of materials processed, stored or combusted.
- E. An amendment to an annual emission inventory questionnaire, containing the documentation required by subsection (B)(3) shall be submitted to the Director by any source whenever it discovers or receives notice, within 2 years of the original submittal, that incorrect or insufficient information was submitted to the Director by a previous questionnaire. If the incorrect or insufficient information resulted in an incorrect annual emissions fee, the Director shall require that additional payment be made or shall apply an amount as a credit to a future annual emissions fee. The submittal of an amendment under this subsection shall not subject the owner or operator to an enforcement action or a civil or criminal penalty if the original submittal of incorrect or insufficient information was due to reasonable cause and not wilful neglect.
- F. The Director may require submittal of supplemental emissions inventory questionnaires for air contaminants pursuant to A.R.S. §§ 49-422, 49-424, and 49-426.03 through 49-426.08.

**R18-2-333. Acid Rain**

- A. The following subparts of 40 CFR 72, Permits Regulation, and all accompanying appendices, adopted as of July 1, 1993 1995, are incorporated by reference. These standards are on file with the Office of the Secretary of State and with the Department and shall be applied by the Department.
  1. Subpart A - Acid Rain Program General Provisions.
  2. Subpart B - Designated Representative.
  3. Subpart C - Acid Rain Applications.
  4. Subpart D - Acid Rain Compliance Plan and Compliance Options.
  5. Subpart E - Acid Rain Permit Contents.
  6. Subpart F - Federal Acid Rain Permit Issuance Procedures.
  7. Subpart G - Acid Rain Phase II Implementation.
  8. Subpart H - Permit Revisions.
  9. Subpart I - Compliance Certification.
- B. When used in 40 CFR 72, "Permitting Authority" means the Department of Environmental Quality and "Administrator" means the Administrator of the United States Environmental Protection Agency.
- C. If the provisions or requirements of the regulations incorporated pursuant to this Section conflict with any of the remaining portions of this Title, the regulations incorporated pursuant to this Section shall apply and take precedence.

**ARTICLE 9. NEW SOURCE PERFORMANCE STANDARDS**

**R18-2-901. Standards of Performance for New Stationary Sources**

Except as provided in R18-2-902 through R18-2-905, the following subparts of 40 CFR 60, New Source Performance Standards (NSPS) and all accompanying appendices, adopted as of July 1, 1993 1995, and no future editions, ~~except for adoption dates as specified below,~~ are incorporated by reference. These standards are on file with the Office of the Secretary of State and with the Department and shall be applied by the Department.

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1. Subpart A - General Provisions.
2. Subpart D - Fossil-Fuel Fired Steam Generators for Which Construction is Commenced After August 17, 1971.
3. Subpart Da - Electric Utility Steam Generating Units for Which Construction is Commenced After September 18, 1978.
4. Subpart Db - Industrial-Commercial-Institutional Steam Generating Units.
5. Subpart Dc - Small Industrial-Commercial-Institutional Steam Generating Units.
6. Subpart E - Incinerators.
7. Subpart Ea - Municipal Waste Combustors.
8. Subpart F - Portland Cement Plants.
9. Subpart G - Nitric Acid Plants.
10. Subpart H - Sulfuric Acid Plants.
11. Subpart I - Hot Mix Asphalt Facilities.
12. Subpart J - Petroleum Refineries.
13. Subpart K - Storage Vessels for Petroleum Liquids for Which Construction, Reconstruction, or Modification Commenced After June 11, 1973, and Prior to May 19, 1978.
14. Subpart Ka - Storage Vessels for Petroleum Liquids for Which Construction, Reconstruction, or Modification Commenced After May 18, 1978, and Prior to July 23, 1984.
15. Subpart Kb - Volatile Organic Liquid Storage Vessels (Including Petroleum Liquid Storage Vessels) for Which Construction, Reconstruction, or Modification Commenced after July 23, 1984.
16. Subpart L - Secondary Lead Smelters.
17. Subpart M - Secondary Brass and Bronze Ingot Production Plants.
18. Subpart N - Primary Emissions from Basic Oxygen Process Furnaces for Which Construction is Commenced After June 11, 1973.
19. Subpart Na - Secondary Emissions from Basic Oxygen Process Steelmaking Facilities for Which Construction is Commenced After January 20, 1983.
20. Subpart O - Sewage Treatment Plants.
21. Subpart P - Primary Copper Smelters.
22. Subpart Q - Primary Zinc Smelters.
23. Subpart R - Primary Lead Smelters.
24. Subpart S - Primary Aluminum Reduction Plants.
25. Subpart T - Phosphate Fertilizer Industry: Wet-Process Phosphoric Acid Plants.
26. Subpart U - Phosphate Fertilizer Industry: Superphosphoric Acid Plants.
27. Subpart V - Phosphate Fertilizer Industry: Diammonium Phosphate Plants.
28. Subpart W - Phosphate Fertilizer Industry: Triple Superphosphate Plants.
29. Subpart X - Phosphate Fertilizer Industry: Granular Triple Superphosphate Storage Facilities.
30. Subpart Y - Coal Preparation Plants.
31. Subpart Z - Ferroalloy Production Facilities.
32. Subpart AA - Steel Plants: Electric Arc Furnaces Constructed After October 21, 1974, and On or Before August 17, 1983.
33. Subpart AAa - Steel Plants: Electric Arc Furnaces and Argon-Oxygen Decarburization Vessels Constructed After August 7, 1983.
34. Subpart BB - Kraft Pulp Mills.
35. Subpart CC - Glass Manufacturing Plants.
36. Subpart DD - Grain Elevators.
37. Subpart EE - Surface Coating of Metal Furniture.
38. Subpart GG - Stationary Gas Turbines.
39. Subpart HH - Lime Manufacturing Plants.
40. Subpart KK - Lead-Acid Battery Manufacturing Plants.
41. Subpart LL - Metallic Mineral Processing Plants.
42. Subpart MM - Automobile and Light Duty Truck Surface Coating Operations.
43. Subpart NN - Phosphate Rock Plants.
44. Subpart PP - Ammonium Sulfate Manufacture.
45. Subpart QQ - Graphic Arts Industry: Publication Rotogravure Printing.
46. Subpart RR - Pressure Sensitive Tape and Label Surface Coating Operations.
47. Subpart SS - Industrial Surface Coating: Large Appliances.
48. Subpart TT - Metal Coil Surface Coating.
49. Subpart UU - Asphalt Processing and Asphalt Roofing Manufacture.
50. Subpart VV - Equipment Leaks of VOC in the Synthetic Organic Chemicals Manufacturing Industry.
51. Subpart WW - Beverage Can Surface Coating Industry.
52. Subpart XX - Bulk Gasoline Terminals.
53. Subpart AAA - New Residential Wood Heaters.
54. Subpart BBB - Rubber Tire Manufacturing Industry.
55. Subpart DDD - Volatile Organic Compound (VOC) Emissions from the Polymer Manufacturing Industry.
56. Subpart FFF - Flexible Vinyl and Urethane Coating and Printing.
57. Subpart GGG - Equipment Leaks of VOC in Petroleum Refineries.
58. Subpart HHH - Synthetic Fiber Production Facilities.
59. Subpart III - Volatile Organic Compound (VOC) Emissions from the Synthetic Organic Chemical Manufacturing Industry (SOCMI) Air Oxidation Unit Processes.
60. Subpart JJJ - Petroleum Dry Cleaners.
61. Subpart KKK - Equipment Leaks of VOC from Onshore Natural Gas Processing Plants.
62. Subpart LLL - Onshore Natural Gas Processing; SO<sub>2</sub> Emissions.
63. Subpart NNN - Volatile Organic Compound (VOC) Emissions From Synthetic Organic Chemical Manufacturing Industry (SOCMI) Distillation Operations.
64. Subpart OOO - Nonmetallic Mineral Processing Plants.
65. Subpart PPP - Wool Fiberglass Insulation Manufacturing Plants.
66. Subpart QQQ - VOC Emissions From Petroleum Refinery Wastewater Systems.
67. Subpart RRR - Volatile Organic Compound (VOC) Emissions From Synthetic Organic Chemical Manufacturing Industry (SOCMI) Reactor Processes (58 FR 45962, August 31, 1993).
68. Subpart SSS - Magnetic Tape Coating Facilities.
69. Subpart TTT - Industrial Surface Coating: Surface Coating of Plastic Parts for Business Machines.
70. Subpart UUU - Calciners and Dryers in Mineral Industries.
71. Subpart VVV - Polymeric Coating of Supporting Substrates Facilities.



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**ARTICLE 11. FEDERAL HAZARDOUS AIR POLLUTANTS**

**R18-2-1101. National Emission Standards for Hazardous Air Pollutants (NESHAPs)**

A. Except as provided in R18-2-1102, the following subparts of 40 CFR 61, National Emission Standards for Hazardous Air Pollutants (NESHAPs) and all accompanying appendices, adopted as of July 1, 1993 1995, and no future editions, except for adoption dates as specified below, are incorporated by reference. These standards are on file with the Office of the Secretary of State and with the Department and shall be applied by the Department.

1. Subpart A - General Provisions.
2. Subpart C - Beryllium.
3. Subpart D - Beryllium Rocket Motor Firing.
4. Subpart E - Mercury.
5. Subpart F - Vinyl Chloride.
6. Subpart J - Equipment Leaks (Fugitive Emission Sources) of Benzene.
7. Subpart L - Benzene Emissions from Coke By-Product Recovery Plants.
8. Subpart M - Asbestos.
9. Subpart N - Inorganic Arsenic Emissions from Glass Manufacturing Plants.
10. Subpart O - Inorganic Arsenic Emissions from Primary Copper Smelters.
11. Subpart P - Inorganic Arsenic Emissions from Arsenic Trioxide and Metallic Arsenic Production.
12. Subpart V - Equipment Leaks (Fugitive Emission Sources).
13. Subpart Y - Benzene Emissions From Benzene Storage Vessels.
14. Subpart BB - Benzene Emissions from Benzene Transfer Operations.
15. Subpart FF - Benzene Waste Operations.

B. Except as provided in R18-2-1102, the following subparts of 40 CFR 63, NESHAPs for Source Categories and all accompanying appendices, adopted as of July 1, 1993 1995, and no future editions, except for adoption dates as specified below, are incorporated by reference. These standards are on file with the Office of the Secretary of State and with the Department and shall be applied by the Department.

1. Subpart A - General Provisions.
2. Subpart B - Requirements for Control Technology Determinations for Major Sources in Accordance with Clean Air Act Sections, Sections 112(g) and 112(j) (59 FR 26429, May 20, 1994).

2. 3. Subpart D - Regulations Governing Compliance Extensions for Early Reductions of Hazardous Air Pollutants (58 FR 62543, November 29, 1993).

4. Subpart F - National Emission Standards for Organic Hazardous Air Pollutants from the Synthetic Organic Chemical Manufacturing Industry.

5. Subpart G - National Emission Standards for Organic Hazardous Air Pollutants from the Synthetic Organic Chemical Manufacturing Industry for Process Vents, Storage Vessels, Transfer Operations, and Wastewater.

6. Subpart H - National Emission Standards for Organic Hazardous Air Pollutants for Equipment Leaks.

7. Subpart I - National Emission Standards for Organic Hazardous Air Pollutants for Certain Processes Subject to the Negotiated Regulation for Equipment Leaks.

8. Subpart L - National Emission Standards for Coke Oven Batteries (58 FR 57911, October 27, 1993).

2. Subpart M - National Perchloroethylene Air Emission Standards for Dry Cleaning Facilities (58 FR 49376, September 22, 1993 and 58 FR 66289, December 20, 1993).

10. Subpart N - Hard and Decorative Chromium Electroplating and Chromium Anodizing Tanks.

11. Subpart O - Ethylene Oxide Emissions Standards for Sterilization Facilities.

12. Subpart Q - Industrial Process Cooling Towers.

13. Subpart T - Halogenated Solvent Cleaning.

14. Subpart W - Epoxy Resins Production and Non-Nylon Polyamides Production.

15. Subpart X - Secondary Lead Smelting.

16. Subpart EE - Magnetic Tape Manufacturing Operations.

**A2. APPENDIX 2. REPEALED TEST METHODS AND PROTOCOLS**

The following test methods and protocols are approved for use as directed by the Department pursuant to this Chapter. These standards are incorporated by reference as of July 1, 1995 (and no future amendments), except for incorporation dates specifically provided. These standards are on file with the Department and with the Office of the Secretary of State.

1. 40 CFR 51, Appendix M.
2. 40 CFR 60, all appendices.
3. 40 CFR 61, all appendices.
4. 40 CFR 63, all appendices.
5. 40 CFR 75, all appendices.
6. The Department's "Arizona Testing Manual for Air Pollutant Emissions," amended as of March 1992 (and no future editions).

**NOTICE OF FINAL RULEMAKING**

**TITLE 19. ALCOHOL, HORSE AND DOG RACING, LOTTERY, AND GAMING**

**CHAPTER 3. ARIZONA STATE LOTTERY COMMISSION**

**PREAMBLE**

**1. Sections Affected**

R19-3-306  
R19-3-307  
R19-3-308

**Rulemaking Action**

New Section  
New Section  
New Section

**2. The specific authority for the rulemaking, including both the authorizing statute (general) and the statutes the rules are implementing (specific):**

Authorizing statute: A.R.S. § 5-504(B)

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**3. The effective date of the rules:**

December 6, 1995

**4. A list of all previous notices appearing in the Register addressing the final rule:**

**Notice of Rulemaking Docket Opening:**

1 A.A.R. 1442, August 25, 1995

**Notice of Proposed Rulemaking:**

1 A.A.R. 1832, October 13, 1995

**5. The name and address of agency personnel with whom persons may communicate regarding the rule:**

Name: Mr. Sam Wakasugi, Acting Executive Director

Address: Arizona State Lottery Commission  
4740 East University  
Phoenix, Arizona 85034

Telephone: (602) 921-4400

**6. An explanation of the rule, including the agency's reasons for initiating the rule:**

These rules set forth provisions unique to the conduct of the Arizona's Lottery's instant games. The provisions of these rules are necessary to implement the requirements of A.R.S. § 5-504(B) which have not been specified generically in R19-3-301. The unique provisions described in these rules are the nature and location of play symbols, the ticket number, the validation code, the prize denominations, and the method of selecting a winning ticket.

**7. A showing of good cause why the rule is necessary to promote a statewide interest if the rule will diminish a previous grant of authority of a political subdivision of this state:**

Not applicable.

**8. The summary of the economic, small business, and consumer impact:**

These games will provide our players with a larger variety of instant games with a potential increase in sales. The only impact these rules have upon Lottery retailers is to specify how they determine if a ticket is a winning ticket and, if so, the prize amount.

**9. A description of the changes between the proposed rules, including supplemental notices, and final rules (if applicable):**

R19-3-307: "Double 21"

D. "Validation" was corrected to read "validations".

E. The following sentence was added: If the ticket holder's "YOUR HAND" gets "21" in either "Game 1", "Game 2", or "Game 3", the player wins double the prize shown for that game." In the prize structure, "\$20 + (\$10/"21")" was corrected to read "\$20 + (\$10 w/ "21")".

R19-3-308: "Match the House"

E. In the proposed version, there is no closing parenthesis -- ")" -- at the end of the game. The final version includes the closed parenthesis.

**10. A summary of the principal comments and the agency response to them:**

No comments were received by the agency.

**11. Any other matters prescribed by statute that are applicable to the specific agency or to any specific rule or class of rules:**

Not applicable.

**12. Incorporations by reference and their location in the rules:**

None.

**13. Was this rule previously adopted as an emergency rule?:**

No.

**14. The full text of the rule follows:**

**TITLE 19. ALCOHOL, HORSE AND DOG RACING, LOTTERY, AND GAMING**

**CHAPTER 3. ARIZONA STATE LOTTERY COMMISSION**

**ARTICLE 3. INSTANT LOTTERY GAMES**

R19-3-306. "Joker's Wild"

R19-3-307. "Double 21"

R19-3-308. "Match the House"

**ARTICLE 3. INSTANT LOTTERY GAMES**

**R19-3-306. "Joker's Wild"**














**A. Four play symbols, which are in a horizontal row, appear under the latex in the play area located on the center right portion of the ticket with "YOUR CARD" printed below each play symbol and are one of the following play spots and captions:**





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- B.** One winning number symbol appears on the upper-right portion of the play area with "DEALER'S CARD" printed above and is one of the following play spots and captions:


	
	
	
	
	
	
	




- C.** A pack-ticket number beginning with 200001 is located in lower-left portion on the back of the ticket.  
**D.** Prize symbol captions correspond with and verify each of the prize symbols as follows:





Prize Symbol	Caption
\$1	ONEDOL
\$2	TWODOL
\$5	FIVEDOL
\$10	TENDOL
\$25	TWFDOL
\$50	FTYDOL
\$500	FIVHUND
\$1,000	ONETHOU

- E.** The retailer validation code verifies instant winners of \$1, \$2, \$5, \$10, \$25, \$50, or \$500. The retailer validation code which corresponds with and verifies each of these winners is as follows:

ONE = \$1	TEN = \$10
TWO = \$2	TWF = \$25
FIV = \$5	FFY = \$50
	FHN = \$500

- F.** A prize winner in the "JOKER'S WILD" instant game is determined by removing the latex from the play area on the front of the ticket to determine the 4 play symbols and the winning number symbol. Neither the retailer-validation code (or any portion thereof), the pack-ticket number (or any portion thereof), nor the validation number (or any portion thereof) are play symbols and are not usable or playable as such. If the player's "YOUR CARD" symbol matches the "DEALER'S CARD" symbol, the player wins the prize amount directly under the play symbol. If a  appears in the winning symbol play spot, the player automatically wins the prize indicated. There may be 4 ways to win on a ticket. The prizes are as follows:

\$1	=	\$1 (one dollar) or
\$1 (w/  )	=	\$1 (one dollar) or
\$2	=	\$2 (two dollars) or
\$1 + (\$1 w/  )	=	\$2 (two dollars) or
\$2 (w/  )	=	\$2 (two dollars) or
\$1 + \$1 + \$1 + \$2	=	\$5 (five dollars) or
\$2 + \$2 + \$1	=	\$5 (five dollars) or

\$5 (w/  )	=	\$5 (five dollars) or
\$5 + \$2 + \$2 + \$1	=	\$10 (ten dollars) or
\$10 (w/  )	=	\$10 (ten dollars) or
\$5 + \$5 + \$5 + \$10	=	\$25 (twenty-five dollars) or
\$25 + (w/  )	=	\$25 (twenty-five dollars) or
\$25 + \$10 + \$10 + \$5	=	\$50 (fifty dollars) or
\$50 (w/  )	=	\$50 (fifty dollars) or
\$500	=	\$500 (five-hundred dollars) or
\$1,000	=	\$1,000 (one-thousand dollars)

**R19-3-307. "Double 21"**

- A.** In the latex play area located on the right side of the ticket, 3 play symbols appear in a vertical row with "YOUR HAND" printed above and will be one of the following play symbols: "13", "14", "15", "16", "17", "18", "19", "20", or "21" with confirming captions. Three play symbols appear in a vertical row with "HOUSE HAND" printed above and will be one of the following play symbols "12", "13", "14", "15", "16", "17", "18", "19", or "20" with confirming captions. The captions are as follows:

Play Symbol	Caption
12	TLV
13	THN
14	FRN
15	ETN
16	SXT
17	SVT
18	EGN
19	NIT
20	TWY
21	DBL

- B.** Three prize symbols appear in a vertical row with "PRIZE" printed above and are one of the following: "\$1", "\$2", "\$5", "\$10", "\$20", "\$40", "\$250", and "\$2,000" with confirming captions. The prize symbols and confirming captions are as follows:

Prize Symbol	Caption
\$1	ONEDOL
\$2	TWODOL
\$5	FIVEDOL
\$10	TENDOL
\$20	TWYDOL
\$40	FRYDOL
\$250	2HUND50
\$2,000	TWOTHOU

- C.** A pack-ticket number is located on the lower-left side of the back of the ticket and begins with 300001.

- D.** The retailer-validation code verifies instant winners of \$1, \$2, \$3, \$5, \$10, \$15, \$40, and \$250. The retailer-validation code which corresponds with and verifies each of these winners is as follows:

ONE = \$1	TEN = \$10
TWO = \$2	FTN = \$15
THR = \$3	FTY = \$40
FIV = \$5	THF = \$250

- E.** A prize winner in the "DOUBLE 21" instant game is determined by removing the latex from the play area on the front of the ticket to determine the 2 play symbols and prize symbol identified as "Game 1", the 2 play symbols and prize symbol identified as "Game 2", and the 2 play symbols and

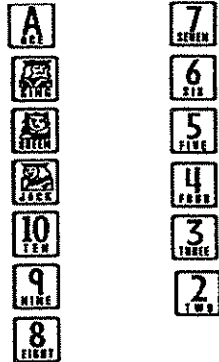
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prize symbol identified as "Game 3". Neither the retailer-validation code (or any portion thereof), the pack-ticket number (or any portion thereof), nor the validation number (or any portion thereof) are play symbols or prize symbols and are not usable or playable as such. If the ticket holder's "YOUR HAND" beats "HOUSE HAND" in either "Game 1", "Game 2", or "Game 3", the player wins the prize shown for that game. If the ticket holder's "YOUR HAND" gets "21" in either "Game 1", "Game 2", or "Game 3", the player wins double the prize shown for that game. There may be 3 winning games on a ticket. The prizes are as follows:

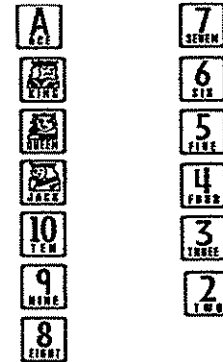
\$1	=	\$1 (one dollar) or
\$1 + \$1	=	\$2 (one dollars) or
\$1 (w/ "21")	=	\$2 (two dollars) or
\$2	=	\$2 (two dollars) or
\$1 + \$1 + \$1	=	\$3 (three dollars) or
\$1 + (\$1 w/ "21")	=	\$3 (three dollars) or
\$5	=	\$5 (five dollars) or
\$2 + \$2 + \$1	=	\$5 (five dollars) or
\$1 + (\$2 w/ "21")	=	\$5 (five dollars) or
\$5 + \$5	=	\$10 (ten dollars) or
\$5 + \$5 + \$5	=	\$15 (fifteen dollars) or
\$5 + (\$5 w/ "21")	=	\$15 (fifteen dollars) or
\$40	=	\$40 (forty dollars)
\$20 + (\$10 w/ "21")	=	\$40 (forty dollars)
\$250	=	\$250 (two-hundred fifty dollars) or
\$2,000	=	\$2,000 (two thousand dollars)

**R19-3-308. "Match the House"**

- A. Four play symbols, which are in a horizontal row, appear under the latex in the play area located on the center portion of the ticket with "YOUR CARD" printed above each play symbol and are one of the following play spots and captions:



- B. One winning number symbol appears on the upper-center portion of the play area with "HOUSE CARD" printed above and is one of the play spots:



- C. A pack-ticket number beginning with 400001 is located in lower-left portion on the back of the ticket.

- D. Prize symbol captions correspond with and verify each of the prize symbols as follows:

Prize Symbol	Caption
\$1	ONEDOL
\$2	TWODOL
\$3	THRDOL
\$5	FIVEDOL
\$10	TENDOL
\$50	FTYDOL
\$100	ONEHUND
\$2,000	TWOTHOU

- E. The retailer-validation code verifies instant winners of \$1, \$2, \$5, \$10, \$20, \$50, or \$100. The retailer-validation code which corresponds with and verifies each of these winners is as follows:

ONE = \$1	TEN = \$10
TWO = \$2	TWY = \$20
FIV = \$5	FFY = \$50
ONH = \$100	

- F. A prize winner in the "MATCH THE HOUSE" instant game is determined by removing the latex from the play area on the front of the ticket to determine the 4 play symbols and the winning number symbol. Neither the retailer-validation code (or any portion thereof), the pack-ticket number (or any portion thereof) are play symbols and are not usable as such. If the player's "YOUR CARD" symbol matches the "HOUSE CARD" symbol, the player wins the prize amount directly under the play symbol. There may be 4 ways to win on a ticket:

\$1	=	\$1 (one dollar) or
\$2	=	\$2 (two dollars) or
\$1 + \$1	=	\$2 (two dollars) or
\$2 + \$2 + \$1	=	\$5 (five dollars) or
\$2 + \$3	=	\$5 (five dollars) or
\$5 + \$5	=	\$10 (ten dollars) or
\$5 + \$2 + \$2 + \$1	=	\$10 (ten dollars) or
\$5 + \$5 + \$10	=	\$20 (twenty dollars) or
\$10 + \$5 + \$3 + \$2	=	\$20 (twenty dollars) or
\$50	=	\$50 (fifty dollars) or
\$100	=	\$100 (one hundred dollars) or
\$2,000	=	\$2,000 (two thousand dollars)

NOTICE OF FINAL RULEMAKING

TITLE 20. PROFESSIONS AND OCCUPATIONS

CHAPTER 6. DEPARTMENT OF INSURANCE

PREAMBLE

1. Sections Affected Rulemaking Action  
R20-6-307 Amend
2. The specific authority for the rulemaking, including both the authorizing statute (general) and the statutes the rules are implementing (specific):  
Authorizing statutes: A.R.S. § 20-143  
Implementing statutes: A.R.S. §§ 20-169, 20-211(C), 20-220, 20-261, 20-261.01, 20-261.02, 20-505, 20-508, 20-509, 20-516, and 20-732.
3. The effective date of the rule:  
January 1, 1996
4. A list of all previous notices appearing in the register addressing the final rule:  
Notice of Rulemaking Docket Opening:  
1 A.A.R. 252, March 31, 1995  
Notice of Proposed Rulemaking:  
1 A.A.R. 1018, July 7, 1995
5. The name and address of agency personnel with whom persons may communicate regarding the accuracy of the economic, small business, and consumer impact statement:  
Name: Gregory Y. Harris  
Address: Department of Insurance  
2910 North 44th Street, Suite 210  
Phoenix, Arizona 85018  
Telephone: (602) 912-8451  
Fax: (602) 912-8452

6. An explanation of the rule, including the agency's reasons for initiating the rule:

Reinsurance provides the mechanism through which an insurer transfers all or a portion of the insurance risks it has assumed to another insurer in return for a premium payment. The insurance industry generally refers to the insurer transferring the risk as the "ceding" insurer and the insurer accepting the risk transfer as the "assuming" insurer or reinsurer.

Reinsurance transactions play an integral part in the underwriting and spreading of risk. Reinsurance enables insurers to protect themselves from losses and to spread the risk of loss much the way primary insurance enables risks to be spread. Reinsurance that effects an actual transfer or assumption of risk also enables insurers to make adjustments to their statutory financial statements of assets and liabilities for credit to be taken for ceded reinsurance.

Current law permits a domestic insurer to claim a credit for reinsurance ceded either as an asset or as a deduction from liability on its annual statement filed pursuant to A.R.S. § 20-223. Thus, the evaluation of the quality of the ceding insurer's reinsurance plays an important role in the monitoring of the insurer's financial condition by the Department of Insurance (the "Department"). The provisions of A.R.S. §§ 20-169 and 20-220 empower the Director to take action against an insurer found to be in a financially hazardous condition. The provisions of A.R.S. §§ 20-261, 20-261.01, 20-261.02, and 20-732 require domestic insurers to submit certain proposed reinsurance agreements to the Director for approval. Further, the provisions of A.R.S. § 20-505 require the Director to determine the liabilities of insurers, including life and disability insurers.

Taken together, these provisions of 20 A.A.C. 6 require the Department to review reinsurance agreements to determine the manner in which related credits or liabilities may be recorded in a ceding insurer's financial statements. The implementing statutes dictate that credits or liabilities may be recorded only if a reinsurance agreement effects an actual shift or transfer of risk.

In 1992, the Department adopted the current rule regarding life reinsurance agreements only. The rule prescribes the standards used by the Department to evaluate life reinsurance agreements to determine whether credits or liabilities may be recorded as a result of a reinsurance agreement.

The Department seeks to amend the current rule and to augment it with more comprehensive provisions that address both life and disability reinsurance agreements. The proposed revisions more thoroughly express the standards to be used by the Department to assess the risk transfer effects of both life and disability reinsurance agreements.

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The Department believes that the proposed amendment of this rule represents the policy adopted by the Legislature through the enactment of the credit for reinsurance statutes. Thus, the Department seeks to adopt this rule because of the benefits to be realized both by consumers and the industry from the stability fostered through accounting practices that encourage accurate reporting of financial data.

The National Association of Insurance Commissioners (the "NAIC"), an association of the chief insurance regulatory officials of the United States, has established an accreditation program that specifies minimum standards of financial solvency regulation. In 1993, the NAIC granted the Insurance Department's accreditation application. The proposed amendment has been designated by the NAIC as an accreditation maintenance requirement effective January 1, 1996. As such, the proposed amendment to the rules implements current NAIC standards to be followed by insurance regulators during the review of life and disability reinsurance agreements.

Virtually every insurance regulator in the country follows the NAIC accreditation standards. These standards provide the means by which insurers receive consistent scrutiny throughout the country. In the process the insurance market achieves a level of reliability and integrity by virtue of the common approach taken by regulators who participate in the accreditation system. Thus, domestic insurers can function across state lines confident of substantially similar levels of treatment by regulators in other jurisdictions. Further, a domestic insurer can be confident that the judgments made by this Department will be given deference. A domestic insurer will not be burdened to demonstrate its relative financial strength entirely anew in every jurisdiction in which the insurer transacts or seeks to transact business. In addition, consumers can be confident that an insurer marketing a product in Arizona but domiciled elsewhere has had its financial condition evaluated under standards substantially similar to those employed by the Department.

Arizona's use of insurer solvency evaluation criteria that is consistent with the laws and rules of other states minimizes additional filings in each state in which an insurer is authorized to transact insurance. Complying with inconsistent standards among states would be extremely burdensome, inconvenient, and expensive for insurers. Consequently, Arizona insurers want Arizona to maintain its accreditation standing.

7. **A showing of good cause why the rule is necessary to promote a statewide interest if the rule will diminish a previous grant of authority of a political subdivision of this state:**

Not applicable.

8. **The preliminary summary of the economic, small business, and consumer impact:**

The principal impact of the rule will fall upon insurers, the Department, and only incidentally upon consumers.

Insurers will feel the impact through the Department's articulation of the standards under which proposed reinsurance agreements will be evaluated to determine if an agreement effects a genuine transfer of risk. If a reinsurance agreement does not genuinely transfer risk, an insurer will not be permitted to gain recognition of claimed assets or reductions in liabilities in its financial statements. Were an insurer permitted to take credit or reduce liabilities for reinsurance agreements that do not effect a genuine transfer of risk, the insurer could artificially overstate its financial strength by inflating its assets or understating its liabilities, thus masking the possibility of the insurer's financial failure. This sequence of events could be catastrophic for the insurer's policyholders and shareholders, for claimants under its insurance policies, and for the taxpayers.

With insurers and the Department applying statutory accounting standards that lead to a more consistent approach to the evaluation of reinsurance agreements, the examination process undertaken by the Department should be more efficient. The use of this fully articulated measure to evaluate proposed reinsurance agreements and agreements recorded on a insurer's financial statements will encourage insurers to enter into acceptable reinsurance transactions. As a consequence, future financial difficulties will be more easily and timely identified.

Consumers will benefit from this rule because the methodology imposed upon insurers for the recording of assets or reductions of liabilities will serve to ensure the accurate recognition of the financial strength of insurers. Insurance consumers will also be spared the costs of multiple filings and other compliance costs which would be imposed by other states requiring an insurer to comply with disparate accounting and solvency statutes or rules. In addition, because of the methodology dictated by this rule, costs borne by the public when an insurer fails should decrease due to the steps taken to prevent failure.

9. **A description of the changes between the proposed rule, including supplemental notices, and final rules (if applicable):**

All changes made to the final rule were made to improve the clarity of the rule. The final rule contains no substantive changes from the rule as proposed.

10. **A summary of the principal comments and the agency response to them:**

The Department received 2 comments during the oral proceeding concerning the rule.

First, 1 comment addressed the applicability of the rule to assuming reinsurers. Specifically, this comment addressed whether the rule would apply to the manner in which domestic life and disability reinsurers maintain financial statements with respect to business being assumed, rather than being ceded, by these reinsurers. As stated in subsection (C), the rule's accounting requirements apply to the accounting entries made by insurers regarding reinsurance ceded rather than reinsurance assumed. Based upon this clarification of the rule, the comment was withdrawn at the oral proceeding.

The 2nd comment involved subsection (C)(1)(h) of the rule, relating to settlement provisions of reinsurance agreements. The rule addresses the statutory requirement that a ceding insurer's statutory accounting of its financial condition accurately reflect the economic reality of a reinsurance transaction. The rule permits the Director to carefully examine a reinsurance agreement to determine if the agreement contains a term that negates the transfer of risk necessary for the agreement to have economic reality. The experi-

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ence of the Director and the Department suggests that reinsurance agreements that contain terms that permit settlement to occur less frequently than quarterly or permit payments to be made more than 90 days after settlement may not have economic reality.

The rule does not categorically prohibit a ceding insurer from making financial statement entries to reflect the effect of a reinsurance agreement if the agreement giving rise to the entries contains a settlement provision of the kind described in subsection (C)(1)(h). The facts underlying a specific transaction may demonstrate that a reinsurance agreement that contains delayed settlement or payment terms has economic reality. The rule therefore permits the Director to exercise the discretion to permit a ceding insurer to reduce a liability or establish an asset even if an agreement contains a settlement term meeting the description prescribed by subsection (C)(1)(h), provided that the ceding insurer can demonstrate the economic necessity of the delayed settlement term.

Based upon this clarification of the discretionary nature of the rule, the comment was withdrawn at the oral proceeding.

11. Any other matters prescribed by statute that are applicable to the specific agency or to any specific rule or class of rules:  
Not applicable.
12. Incorporations by reference and their location in the rules:  
Not applicable.
13. Was this rule ever previously adopted as an emergency rule:  
No.
14. The full text of the rules follows:

**TITLE 20. PROFESSIONS AND OCCUPATIONS**

**CHAPTER 6. DEPARTMENT OF INSURANCE**

**ARTICLE 3. FINANCIAL PROVISIONS AND PROCEDURES**

R20-6-307. Life and Disability Reinsurance Agreements

**ARTICLE 3. FINANCIAL PROVISIONS AND PROCEDURES**

R20-6-307. Life and Disability Reinsurance Agreements

A. Scope and Applicability. This rule shall apply applies to all domestic life and disability insurers and reinsurers, and to all other licensed life and disability insurers and accredited reinsurers who that are not subject to a substantially similar rule in their domiciliary state jurisdictions of domicile. This rule shall also apply applies to the disability business of licensed property and casualty insurers. "Substantially similar" standards means life reinsurance agreement standards which the Department determines equal or exceed the standards of this rule. This rule does not apply to assumption reinsurance, yearly renewable term reinsurance, or nonproportional stop loss or catastrophe reinsurance, or similar forms of nonproportional reinsurance.

**B. Definitions**

1. "Agreement" means a reinsurance agreement and any amendment to a reinsurance agreement.
2. "Credit Quality" means the risk that invested assets supporting the reinsured business will decrease in value but excludes decreases to changes in interest rate.
3. "Department" means the Arizona Department of Insurance.
4. "Director" means the Director of the Arizona Department of Insurance.
5. "Disintermediation" means the risk that interest rates will rise and policy loans and surrenders will increase or maturing contracts will not renew at anticipated rates of renewal.
6. "Lapse" means the risk that a policy will voluntarily terminate before the recoupment of a statutory surplus strain experienced at issuance of the policy.
7. "Reinvestment" means the risk that interest rates will fall and funds reinvested will therefore earn less than expected.

**B.C. Accounting Requirements**

1. Unless authorized by the director, no an life insurer subject to this rule shall not, establish any asset for reinsurance ceded, reduce any liability or establish any asset in any statutory financial statement filed with the Department if, by the terms of the reinsurance agreement, in substance or in effect, any of the following conditions exist:
  1. The effect of the reinsurance agreement is to transfer deficiency reserves or excess interest reserves to the reinsurer for a risk charge against the ceding insurer and the agreement does not provide for participation by the reinsurer that is significant relative to the reserves transferred to the reinsurer for one or more of the following risks: mortality, morbidity, investment, or surrender benefit;
    - a. Renewal expense allowances provided or to be provided to the ceding insurer by the reinsurer in any accounting period are not sufficient to cover the ceding insurer's allocable renewal expenses anticipated at the time the business is reinsured on the portion of the business reinsured, unless a liability is established for the present value of the shortfall using assumptions equal to the applicable statutory reserve basis on the business reinsured.
  2. The reserve credit taken by the ceding insurer is not in compliance with the applicable provisions of A.R.S. Title 20 and the rules promulgated pursuant thereto;
  3. The reserve credit taken by the ceding insurer is greater than the underlying reserve of the ceding insurer supporting the policy obligations transferred under the reinsurance agreement.
- 4.b. The ceding insurer is required to reimburse the reinsurer for negative experience under the reinsurance agreement, except that neither the offset of the ceding insurer's experience refunds against the reinsurer's prior years' losses, nor payment by the ceding insurer of an amount equal to the reinsurer's prior years' losses upon voluntary termination of in force reinsurance by the ceding insurer, shall be considered such a reimbursement to the reinsurer for negative experience. Neither the offset of the ceding

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- insurer's experience refunds against current and prior years' losses, nor payment by the ceding insurer of an amount equal to the reinsurer's current and prior years' losses upon voluntary termination of in-force reinsurance by the ceding insurer, shall be considered a reimbursement to the reinsurer for negative experience.
- 5.c. The ceding insurer may be deprived of surplus or assets at the reinsurer's option or automatically upon the occurrence of a specified event, including the insolvency of the ceding insurer, except that termination of reinsurance agreement by the reinsurer for nonpayment of reinsurance premiums shall not be considered to be such a deprivation of surplus. Termination of the agreement by the reinsurer for nonpayment of reinsurance premiums or other amounts due shall not be considered a deprivation of surplus or assets within the meaning of this subsection.
- 6.d. The ceding insurer shall is required, at specific scheduled times scheduled in the agreement, to terminate the agreement or automatically recapture automatically all or part of the reinsurance ceded.
7. ~~No cash payment is due from the reinsurer during the term of the reinsurance agreement, with all settlements prior to the termination date of the agreement made only as adjustments to a reinsurance account, but no funds attributable to such account are made available to the ceding insurer for the payment of the benefits; or~~
- 8.c. The reinsurance agreement ceding insurer may be required to pay ~~require payment by the ceding insurer to the reinsurer of amounts other than from income reasonably expected from the reinsured policies.~~
- f. Significant risks inherent in the business reinsured are not transferred to the reinsurer. Table A identifies the risks deemed significant for representative types of business.
- g. The credit quality, reinvestment, or disintermediation risk is significant for the business reinsured and the ceding company does not transfer the underlying assets to the reinsurer, segregate the underlying assets in a trust or escrow account, or otherwise segregate the underlying assets. The assets that support the reserves for classes of business that do not have a significant credit quality, reinvestment, or disintermediation risk, or for long-term care or long-term disability insurance, traditional non-par permanent, traditional par permanent, adjustable premium permanent, indeterminate premium permanent, or universal life fixed premium with no dump-in premiums allowed, may be held by the ceding company without segregation. To determine the reserves for classes of business, the supporting assets of which may be held without being segregated, the reserve interest rate adjustment formula shall reflect the ceding company's investment earnings and
- incorporate all realized and unrealized gains and losses reported in the ceding insurer's statutory financial statement.
- h. Settlements are made less frequently than quarterly or payments due from the reinsurer are not made in cash within 90 days of the settlement date.
- i. The ceding insurer is required to make representations or warranties unrelated to the business reinsured.
- j. The ceding insurer is required to make representations or warranties related to future performance of the business reinsured.
2. An agreement entered into after the effective date of this rule to reinsure business issued before the effective date of the agreement shall be filed by the ceding insurer with the director within 30 days after execution of the agreement. Each filing shall be accompanied by a description of the corresponding reduction in liabilities or other credit for reinsurance, and any other financial impact of the agreement, reported in the ceding insurer's statutory financial statements. When an increase in surplus net of federal income tax results from an agreement falling under this subsection, the ceding insurer shall separately identify the increase as a surplus item in the aggregate write-ins for gains and losses in surplus in the Capital and Surplus account of the ceding insurer's statutory financial statement. As earnings emerge from the business reinsured, the ceding insurer shall report in its financial statement recognition of surplus increase as income on a net of tax basis as reinsurance ceded.
- C.D. Written Agreements**
1. ~~No ceding life insurer subject to this rule~~ A ceding insurer shall not reduce any liability or establish any asset in any statutory financial statement filed with the Department on the basis of any reinsurance agreement or amendment thereto, unless the ceding insurer and the reinsurer have executed an agreement, amendment, or a binding letter of intent has been executed by both all parties by the "as of" date of the statutory financial statement.
2. ~~A reinsurance or an amendment thereto shall be executed within 90 days from the execution date of the letter of intent for~~ A ceding insurer shall not be allowed a credit to be granted for the reinsurance ceded based on a letter of intent unless the ceding insurer and the reinsurer execute an agreement within 90 days from the execution date of the letter of intent.
3. The agreement shall provide that:
- a. The agreement constitutes the entire contract between the parties with respect to the business reinsured, and there are no understandings between the parties other than as expressed in the agreement; and
- b. Any change or modification to the agreement shall be void unless made by written amendment signed by all parties.



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**Table A**

Risk Categories

(a) Morbidity.

(b) Mortality.

(c) Lapse.

(d) Credit Quality

(e) Reinvestment

(f) Disintermediation

	a	b	c	d	e	f
<u>Disability Insurance, other than long-term care or long-term disability insurance.</u>	±	0	±	0	0	0
<u>Long-term care or long-term disability insurance</u>	±	0	±	±	±	0
<u>Immediate Annuities</u>	0	±	0	±	±	0
<u>Single Premium Deferred Annuities</u>	0	0	±	±	±	±
<u>Flexible Premium Deferred Annuities</u>	0	0	±	±	±	±
<u>Guaranteed Interest Contracts</u>	0	0	0	±	±	±
<u>Other Annuity Deposit Business</u>	0	0	±	±	±	±
<u>Single Premium Whole Life</u>	0	±	±	±	±	±
<u>Traditional Non-par Permanent Life</u>	0	±	±	±	±	±
<u>Traditional Non-par Term Life</u>	0	±	±	0	0	0
<u>Traditional Par Permanent Life</u>	0	±	±	±	±	±
<u>Traditional Par Term Life</u>	0	±	±	0	0	0
<u>Adjustable Premium Permanent Life</u>	0	±	±	±	±	±
<u>Indeterminate Premium Permanent Life</u>	0	±	±	±	±	±
<u>Universal Life Flexible Premium</u>	0	±	±	±	±	±
<u>Universal Life Fixed Premium with dump-in premiums allowed</u>	0	±	±	±	±	±

± - Significant

0 - Insignificant